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**MEDICARE'S SHARE IN
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MEDICARE'S SHARE IN U.S. PHYSICIANS' REVENUES

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The purpose of this Background Paper series is to make available materials prepared for use by the members of the Physician Payment Review Commission in making their recommendations to Congress. The papers published in this series are background analyses and do not contain Commission recommendations.

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ABSTRACT

Standard estimates of national health expenditures for 1987 show Medicare payments to physicians equalled 22 percent of U.S. physicians' gross revenues from practice (Letsch, Levit, and Waldo, 1988). Most statements about Medicare's role in U.S. physicians' income quote this statistic. However, adding Medicare coinsurance, deductible, and balance billing raises the portion of physicians' revenues from Medicare-covered services in 1987 to 28 percent. By excluding from consideration pediatricians and obstetrician/gynecologists, who see less than one-tenth as many Medicare patients as do typical physicians, this percentage is further increased. In 1987, excluding these two specialties, the contribution of Medicare-covered services to the practice revenues of physicians ⁴⁰ was approximately 33 percent. Thus Medicare's financial significance to American physicians generally is substantially larger than the figure usually cited.

INTRODUCTION

National health expenditure estimates for the United States, which are prepared annually by the Office of the Actuary, Health Care Financing Administration (HCFA), show total U. S. expenditures for physicians' services were \$102.7 billion in 1987. Medicare paid \$22.3 billion, or 21.7 percent of this amount (Letsch, Levit, and Waldo, 1988, p. 118). Total physician expenditures, as measured in these annual estimates, consist of gross business receipts of physician practices (sole proprietorships, partnerships, and corporations) as reported to the Internal Revenue Service plus an estimate of compensation of physicians employed by staff model Health Maintenance Organizations (HMOs). (The HMO compensation equals between one-half and one percent of the total.) Physicians employed by hospitals are excluded. The national health expenditure estimates also exclude limited license practitioners (podiatrists, chiropractors, and so on) who are often included when Medicare uses the word "physicians."

The statistic that Medicare payments are 22 percent of physicians' incomes is widely cited. This figure, although taken directly from the national expenditure estimates, substantially underestimates the true contribution of Medicare-covered services to physicians' practice incomes. This paper presents a more appropriate estimate.

BENEFICIARIES' COST SHARING

Because of cost sharing, Medicare beneficiaries (or their supplemental insurers) make substantial payments for the same services for which Medicare pays physicians. To estimate the share of physicians' revenues coming from Medicare-covered services requires adding in the three components of cost sharing: coinsurance, deductibles, and balance billing. Counting them in Medicare's share of physicians' revenues is appropriate because Medicare rules fully determine coinsurance and deductible amounts and allow for balance billing up to established ceilings.

Coinsurance

Medicare's 20 percent coinsurance means that for every five dollars in expenses to which coinsurance is applicable, Medicare pays four dollars and beneficiaries have one dollar in coinsurance liability. Thus beneficiaries' coinsurance liability equals one-fourth of Medicare's payment to physicians, an amount that totalled \$5.6 billion in 1987. The Physician Payment Review Commission's (PPRC's) 1988 survey of physicians asked physicians the percentage of Medicare coinsurance they actually collect. The responses to this question yield an estimated collection rate of 70 percent of the coinsurance

liability.¹ Thus, physicians received approximately \$3.9 billion from beneficiaries for coinsurance in 1987.

Deductibles

HCFA estimated that 24.3 million Medicare beneficiaries (79 percent of the total) met the \$75 Part B deductible in 1987 (Committee on Ways and Means, 1989, p. 128). HCFA also estimated that payments to physicians approximated 73 percent of total Part B payments in 1987 (Committee on Ways and Means, 1989, p. 132). Assuming then that a similar percentage of deductible payments was for physicians services and applying the 70 percent collection rate², it is estimated that physicians received \$0.9 billion in deductibles from patients who met the deductible. HCFA estimated 6.6 million beneficiaries did not reach the deductible (Committee on Ways and Means, 1989, p. 128). Assuming their expenses for covered Part B charges on average equalled half the \$75 deductible³ and using the same ratios as were used for beneficiaries who reached the deductible, there is an additional \$0.1 billion paid to physicians by beneficiaries who did not meet the deductible. Thus, the total in deductible amounts paid to physicians by all beneficiaries in 1987 approximated \$1.0 billion.

Balance Billing

Balance billing is the term used for charges by physicians on unassigned claims that exceed the amount Medicare allows.

HCFA "Carrier Reasonable Charge and Denial Activity Report" data show \$2.5 billion in balance billing for all Medicare Part B services in 1987. The best estimate is that 94

¹ The estimate of a 70 percent collection rate was computed from survey responses as follows: Within a specialty, each physician's reported collection rate was weighted according to his sampling weight times the percent of his practice composed of Medicare patients (as reported on the survey). Then each specialty was weighted according to its share of 1987 Medicare payments to physicians (as shown in Committee on Ways and Means, 1989, p. 408). The simple, unweighted average of physicians' survey responses was a very similar 69 percent collection rate.

² The PPRC survey did not ask about a collection rate for deductibles. It seems probable physicians treat deductibles in the same way as coinsurance. In any case, a collection rate for deductibles that differed from that for coinsurance by 10 percent would result in a difference in the estimate of physician revenues from deductibles of \$0.1 billion.

³ This assumption is highly uncertain, but can at most lead to an error of \$0.1 billion in physicians' revenues, which is a very small portion of the sums under consideration.

percent of this balance billing was by physicians.⁴ The 1988 PPRC physician survey indicates a collection rate of at least 75 percent on physicians' balance bills.⁵ Applying these figures yields an estimate of \$1.8 billion in balance billing collected by physicians in 1987.

Total Including Cost Sharing

Estimated physician receipts from beneficiaries for the three components of beneficiary cost sharing totaled \$6.7 billion in 1987. Added to the \$22.3 billion estimate of Medicare's own payments to physicians, this gives an estimated total of \$29.0 billion received by physicians for services covered by Medicare. This \$29.0 billion is 28.2 percent of physicians' estimated total 1987 practice income of \$102.7 billion.

SPECIALTIES RARELY SERVING MEDICARE PATIENTS

Some physicians, most notably pediatricians, rarely see Medicare patients. In assessing the importance of Medicare in U.S. physicians' practices, it is appropriate to remove these physicians from consideration, recognizing that Medicare has a very small role in their practice. This section therefore estimates the importance of Medicare among those specialties in which it does have a significant role.

⁴ This estimate is based on the following data: In fiscal year (FY) 1987, physicians and limited license practitioners were responsible for 97 percent of balance billing (Personal communication from staff of Bureau of Program Operations, HCFA). Allowed charges for limited license practitioners in FY 1987 were approximately 3 percent of those for physicians (Committee on Ways and Means, 1989, p. 407). PPRC tabulations of 1986 Part B Medicare Annual Data (BMAD) III files show podiatrists and chiropractors, who together accounted for 2.3 percent of total allowed charges (that is, for the preponderance of charges from limited license practitioners) accounted for a close-to-proportional 2.1 percent of balance billing.

⁵ The survey asked physicians on what percent of unassigned billings they collected *both* the coinsurance and the balance bill. The 75 percent estimate of the balance billing collection rate is based on the answer to this question. The estimate was computed as follows: The response of each physician in a specialty was weighted according to the physicians' sampling weight times the percentage of his practice composed of Medicare patients times the percent of charges on which he balance billed. (Percent of practice composed of Medicare patients and percent of charges balance billed were both reported on the survey.) Each specialty was then weighted according to its share in total balance billing. Two different estimates of specialty shares were used. One was the 1987 share in eight states as shown in a study of balance billing conducted by McMenamin and colleagues for the PPRC. The other was a PPRC tabulation of balance billing by specialty from the 1986 BMAD-III file. Both gave an estimate of a 75 percent collection rate. With no weighting, physicians' mean response was 72 percent.

The finding that the collection rate for balance billing is higher than that for coinsurance is unexpected, for coverage of coinsurance by supplemental insurance is much more common than coverage of balance billing. The explanation may be that physicians generally balance bill only if they expect to collect the balance bill, while coinsurance applies to all services and all beneficiaries, and there may be some beneficiaries from whom the physician has little expectation of collecting and some services for which the coinsurance amount is too small to merit an attempt to collect.

HCFA data (Committee on Ways and Means, 1989, p. 408) show pediatricians and obstetrician/gynecologists accounted for, respectively, 0.1 and 0.7 percent of Medicare allowed charges for physicians' services in 1987. In contrast, AMA data indicate these specialties accounted for approximately 5.1 percent and 9.3 percent, respectively, of all physician revenues in the U.S in 1987.^{6 7}

Together, these two specialties accounted for approximately 14.4 percent of physician revenues, and subtracting that percentage from the \$102.7 billion received by all physicians in 1987 leaves \$87.9 billion as the approximate total practice revenues of all other physicians. Receipts of practitioners in these two specialties from Medicare-covered services were approximately 0.8 percent of \$29.0 billion in 1987, or \$0.2 billion. Thus, physicians in other specialties received approximately \$28.8 billion from Medicare-covered services and had total practice revenues of \$87.9 billion in 1987. In short, approximately 32.8 percent of their revenues came from Medicare-covered services.

CONCLUSION

Revenues from Medicare-covered services accounted for approximately one-third of the 1987 practice revenues of physicians in specialties that see significant numbers of Medicare beneficiaries.⁸ This share is half again as large as the 22 percent figure commonly cited, and if past trends continue, it will grow. Thus, Medicare has a greater ability to influence physicians than is generally recognized.

⁶ These shares are calculated by multiplying the percentage of all U.S. office-based patient-care physicians who are in the specialty in question (from Roback et al., 1988, Table 6) by the ratio of the specialty's mean total practice income per self-employed physician to the mean total practice income per self-employed physician for all specialties. The data on total practice income are from Gonzales, 1989, p. 65.

⁷ These figures lead to the conclusion that Medicare patients accounted for less than 1 percent of practice revenues of pediatricians and for approximately 2 percent of revenues of obstetrician/gynecologists. In comparison, the figure was 28 percent for all physicians.

⁸ Based on work with the data, the margin of error in the estimates of Medicare's share seems to be perhaps 1 or 2 percentage points.

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